115 (g), in the event that the Court should hold the basis of the redeemed Stock Dividend not to be zero, as contended in (1) above.

This alternative contention, if allowed, would result in adding $200,000 to the Taxpayer's income for 1931 in the form of dividend income. This contention was not raised by cross appeal.

The Circuit Court of Appeals held that the Preferred Stock Dividend received in 1931 was not subject to tax under the terms of Section 115 (f) of the Revenue Act of 1928. The Circuit Court of Appeals refused to consider a deficiency *pro tanto* upon the theory that the cost basis of the stock sold to the Corporation by the Taxpayer during the taxable year, and previously received as a Stock Dividend in 1928, was zero, because this point was not raised before nor decided by the Board of Tax Appeals. The Circuit Court of Appeals further refused to consider whether the redemption of the Preferred Stock in 1931 was the equivalent of the distribution of a taxable dividend under Section 115 (g), because the Government did not file a cross appeal from the decision of the Board of Tax Appeals, and further because the Board of Tax Appeals did not find that the redemption of the Preferred Stock in question occurred at such time and in such manner as to make the redemption essentially equivalent to the distribution of a taxable dividend under the provisions of Section 115 (g).

Reason for Not Granting the Writ.

The questions presented do not warrant further consideration by this Court.

Argument on Questions Presented.

I.

Is a dividend by a corporation in its own Preferred Stock, paid to holders of Common Stock when there were other shares of Preferred Stock of the same classification outstanding a part of which were held by others than the common stockholders, a "stock dividend" within the meaning of Section 115 (f) of the Revenue Act of 1928?

Section 115(f) of the Revenue Act of 1928 provides:

"A stock dividend shall not be subject to tax."

The question here presented involves the construction of the above quoted section. It was determined in the negative and in favor of the taxpayers by the Circuit Court of Appeals for the Second Circuit on February 15, 1937 in this case and by the Circuit Court of Appeals for the Seventh Circuit on December 22, 1936 in the case of *Gowran* v. *Commissioner* (87 Fed. (2) 125).

There has been no conflict in the Circuit Courts of Appeals on this question in any case where the Government was attempting to tax stock dividends as income.

The question was first suggested in *Tillotson Manufacturing Company* v. *Commissioner* (27 B. T. A. 913), decided in 1933, but was raised by the taxpayer, not by the Government. The fundamental question in that case was not the taxability of a stock dividend under Section 115 (f) of the Revenue Act, but the proper cost basis for determining capital gain upon the sale of Preferred Stock upon which a Common Stock Dividend had been paid. The Board of Tax Appeals in the *Tillotson* case, reversing the Commissioner, and sustaining the taxpayer, held that a dividend paid by a corporation in its Common Stock on its Preferred

Stock did not diminish the basis of the Preferred Stock. The reason given by the Board for this decision was that the Common Stock Dividend was not exempt from taxation either under the Statute or under the Constitution, and that, therefore, such Common Stock Dividend constituted taxable "income", and so left the cost basis of the Preferred Stock undiminished.

On appeal, the Circuit Court of Appeals for the Sixth Circuit affirmed, stating that the stock dividend Constitutionally was not exempt from taxation. (76 Fed. (2d) 189.) This was in 1935. The decision of that Court, while referring to the Statutory exemption, does not seem to have decided the case on that point.

As will below appear, the result reached by the Board of Tax Appeals and by the Circuit Court of Appeals in the *Tillotson* case was later approved by this Court but not upon the principle that the Stock Dividends were taxable under the Statute when received.

The case of *Koshland v. Helvering* (81 Fed. (2d) 641) was the next case after the *Tillotson* case in the series of Stock Dividend cases. That case was decided on January 20, 1936 by the Circuit Court of Appeals for the Ninth Circuit. That Court did not consider the question of Constitutional exemption but held, reversing the Board, that a common stock dividend on Preferred Stock was specifically exempt from tax under the Statute (Section 115 (f)) and approved the action of the Commissioner in adjusting the cost basis of the Preferred Stock upon which the Stock Dividend was paid.

On Writ of Certiorari in the *Koshland* case (298 U. S. 441) this Court on May 18, 1936 held as follows:

1. That a dividend on Preferred Stock paid in Common Stock of a corporation is "income" under the Sixteenth

Amendment to the Constitution, *whether or not Congress has taxed it as of the time of its receipt.*

2. That where a taxpayer purchased non-voting cumulative Preferred Stock of a corporation upon which a dividend was subsequently paid in Common Stock, and thereafter disposed of such Preferred Stock, there should be no apportionment of cost between Preferred and Common Stock for the purpose of determining gain or loss.

The reasoning of the opinion of this Court in the *Koshland* case was that Congress, having expressly declared in computing capital gain that the "cost" of the asset disposed of shall be deducted from the selling price, the Secretary of the Treasury was without power by Regulation "to add a provision that income derived from the capital asset shall be used to reduce cost." The question of whether or not Congress had exempted such a stock dividend from taxation was not expressly decided. That this Court, however considered such a Stock Dividend to be exempt under the Statute may be fairly inferred from the following language used by this Court in its opinion:

> "Although *Eisner* v. *Macomber* affected only the taxation of dividends declared in the same stock as that presently held by the taxpayer, the Treasury gave the decision a broader interpretation which Congress followed in the Act of 1921. Soon after the passage of that act, this Court pointed out the distinction between a stock dividend which worked no change in the corporate entity, the same interest in the same corporation being represented after the distribution by more shares of precisely the same character, and such a dividend where there had either been changes of corporate identity or a change in the nature of the shares issued as dividends whereby the proportional interest of the stockholder after the distribution was essentially different from his

former interest. *Nevertheless the successive statutes and Treasury regulations respecting taxation of stock dividends remained unaltered.*" (Italics supplied by us.)

The Circuit Court of Appeals for the Second Circuit in the *Pfeiffer* case in commenting upon the above portion of the opinion of this Court stated:

> "This language indicates clear recognition that the exemption contained in the Revenue Act was broader than required by the decision of *Eisner* v. *Macomber,* 252 U. S. 189, and that it is coextensive with that contained in the regulations.
>
> "This fact is amply demonstrated by the background and history of § 115 (f)."

The Circuit Court of Appeals for the Seventh Circuit in the *Gowran* case, and the Circuit Court of Appeals for the Second Circuit in this, the *Pfeiffer* case, both followed what they believed to be the conclusion of this Court as expressed in its opinion in the *Koshland* case.

On October 31, 1936, in the case of *August Horrmann,* 34 B. T. A. 1178, the Board of Tax Appeals, which was the first to raise the question of the taxability of stock dividends under the Statute when received, and the only judicial or semi-judicial branch of the Government which has attempted to tax stock dividends when received, would seem to have definitely reversed its opinion. The Board there said:

> "Whether we are right or wrong in our interpretation of the *Koshland* case, and whether or not the preferred stock dividend of 1922 was income, we are of the opinion that it was not taxable to the stockholders. Of course, if it was a stock dividend, within the compass of *Eisner* v. *MacComber,* it was not income under the Sixteenth Amendment; if it was income, as in the *Koshland* case, it was nevertheless

a stock dividend which was specifically exempt from tax under Section 201 (d) of the Revenue Act of 1921.

This exemption has been of long standing as pointed out in the opinion in the *Koshland* case. All of the Revenue Acts from 1921 to 1934, inclusive, have specifically provided for the exemption and the Treasury regulations over an equally long period of time have broadly held stock dividends nontaxable."

The following propositions would seem to be well established:

1. A dividend paid in the stock of a corporation declaring the dividend is, by common definition, a stock dividend.

2. The Treasury Department, in its official Regulations and Treasury Decisions, and Congress, in its previous Acts, for fourteen years uniformly used the term "stock dividend" as meaning a dividend paid by a corporation in shares of its own stock, although paid in stock of a character different from the stock on which the stock dividend was paid.

3. The Administrative construction of a Statute is entitled to great weight.

4. Taxpayers had a right to rely upon a normal interpretation of the language of a Statute and upon the Administrative construction thereof.

5. Successive reenactments by Congress of a Statutory provision exempting stock dividends from taxation, after such uniform practice on the part of the Treasury Department, are persuasive evidence of Legislative approval of the Administrative construction of such provisions.

6. Section 115 (g) of the Revenue Act of 1928 and the corresponding Sections of other Acts provide for taxation under certain circumstances of the proceeds from the redemption of stock issued as a Stock Dividend. This provision of the Statutes shows that Congress understood that such dividends were not taxable when received, and intended that such dividends should not be taxable when received.

The Circuit Courts of Appeals for three Circuits—the Ninth, the Seventh and the Second—have held that stock dividends of the character involved in this case are not subject to tax under the Statute. The Board of Tax Appeals, we believe, has now reached the same conclusion. This Court, in the *Koshland* case, has already indicated that this was its own view.

These decisions conform to a long and definitely established legislative and administrative policy and confirm the correctness of the position which the Government originally took, and uniformly and continuously has taken before the Board of Tax Appeals, the Circuit Courts of Appeals and this Court, in all cases which preceded the *Gowran* and *Pfeiffer* cases.

The law on this point seems now to be settled. There is no reason, therefore, why this Court should be asked to review the question further.

A reversal of this long-established policy of the Government would result in the infliction of tremendous hardships upon taxpayers who, in shaping their corporate financial policies, have relied for many years upon the plain language of the Statute and upon the Government's own interpretation and enforcement of the Statute.

There is no Constitutional question involved in the question here presented.

Since the decision in the *Koshland* case, in May, 1936, Congress changed the law with respect to the taxation of stock dividends, by an amendment enacted on June 22, 1936, contained in Section 115 (f) (1) of the Revenue Act of 1936, which made stock dividends in the future taxable to the extent that they constitute "income" within the meaning of the Sixteenth Amendment to the Constitution.

It is submitted that this amendment indicates that Congress did not intend to tax stock dividends under the previous statute or is convinced that it did not do so. Thus, beginning with the year 1936, the question of statutory exemption of stock dividends will not arise, and revenue will be collected accordingly.

II.

Is such a Preferred Stock Dividend taxable under the Sixteenth Amendment to the Constitution?

The Circuit Court of Appeals for the Second Circuit in this case did not express an opinion on this point.

The Circuit Court of Appeals for the Seventh Circuit apparently assumed in the *Gowran* case that, by reason of the decision of this Court in the *Koshland* case, the stock dividend in the *Gowran* case must be held to be income which Congress, under the Constitution, might tax.

If this Court agrees that a stock dividend is not subject to tax under the Statute, the taxability of such income under the Constitution need not be decided here, at least so far as concerns the taxability of the Stock Dividend distribu-

tion. If, however, this Court should not agree with the Circuit Court of Appeals that a Stock Dividend is not subject to tax under the Statute, then the question of taxability under the Constitution will be an issue and should be argued before this Court.

A dividend of Preferred Stock on Common Stock, such as was paid in this case, may present a very different situation from that which existed in the *Koshland* case, where there was a dividend of Common Stock paid upon Preferred Stock. It would not seem, however, that this question should be argued on this application.

III.

Should the Circuit Court of Appeals have passed upon the question of the cost basis of the Dividend Stock sold during the taxable year?

The question of the taxability as capital gain of the $200,000 or any part thereof, received by the Taxpayer from the redemption of the 2,000 shares of Preferred Stock received as a Stock Dividend during the year 1928, was not an issue before or decided by the Board of Tax Appeals.

This Court has definitely held in the case of *General Utilities and Operating Company* v. *Helvering*, 296 U. S. 200, that a Circuit Court of Appeals is without authority to decide a question not at issue before or decided by the Board of Tax Appeals. This Court reached the same conclusion in the case of *Helvering* v. *Salvage*, 297 U. S. 106. The Circuit Court of Appeals, therefore, should not have considered or decided in this case the question of cost basis raised by the Government for the first time in its brief submitted to such Court.

IV.

If the Circuit Court of Appeals should have passed upon the cost basis of the Dividend Stock what is the correct cost basis, assuming that such dividend was not subject to tax under the Statute at the time of its receipt?

It was decided, in favor of the taxpayer, by the Circuit Court of Appeals for the Seventh Circuit in the *Gowran* case, that the cost basis of a Preferred Stock Dividend paid on Common Stock was the fair market value of such Preferred Stock when received, and not, as claimed there and here by the Government, zero. In the *Gowran* case a Petition for a Writ of Certiorari was filed in this Court on April 12, 1937. It is assumed that such Petition will be considered at the same time as the Petition in this case. As we will file an *amicus curiae* brief in opposition to the granting of a Writ of Certiorari in the *Gowran* case, in which brief the question above presented will be discussed and reasons given for not granting the Writ, we refrain from discussing such question here at length. We respectfully refer the Court to our brief in the *Gowran* case, so far as the above question is concerned.

V.

Should the Circuit Court of Appeals have held that the proceeds from the redemption of the dividend stock in this case were taxable under Section 115 (g)?

The Board of Tax Appeals held that because the Stock redeemed in 1931 was, as it thought, taxable in 1928, when received, the proceeds from the redemption were not sub-

ject to taxation in 1931 under Section 115 (g) of the Revenue Act.

The Circuit Court of Appeals reversed the Board by holding that a stock dividend is not subject to tax under the Statute when received. The Circuit Court further held, however, that the proceeds from the redemption of stock can be taxed as a dividend under the provisions of Section 115 (g) *only* if the redemption occurs at such time and in such manner as to make the redemption essentially equivalent to the distribution of a taxable dividend and, as the Board did not so find, the Circuit Court refused to sustain the contention of the Government that the redemption in question was the equivalent of a taxable dividend.

The Board did not find as a matter of fact or as a matter of law, that this redemption occurred at such time and in such manner as to make the redemption essentially equivalent to the distribution of a taxable dividend. The Commissioner did not file a cross appeal and so did not place the decision of the Board in this respect in issue before the Circuit Court.

There is certainly no presumption that a redemption of a Stock Dividend is equivalent to a taxable dividend. (*Commissioner* v. *Brown*, 69 Fed. (2) 602; *Commissioner* v. *Rockwood*, 82 Fed. (2) 359; *August Horrmann, supra.*)

The Government did not ask the Circuit Court to remand this case to the Board of Tax Appeals for a determination with respect to the application of Section 115 (g) to the circumstances of this case. No authority is cited by the Government in its brief before this Court that this case may now be so remanded. The effect of so remanding this case would be to bring up again a question which was decided by the Board from which decision no cross appeal was taken. What the Government asked of the Circuit Court on the argument before that Court was to hold, as

a matter of law, that the redemption was essentially equivalent to the distribution of a taxable dividend (Govt. Brief before the C. C. A. p. 24). This the Circuit Court of Appeals refused to do.

It should, further, be stated that this issue does not involve an important question of Federal law nor a question which would be helpful in the decision of other cases, because the application of Section 115 (g) is dependent entirely upon the facts of each individual case.

Conclusion.

There is no important question of law here presented which needs further settlement by this court.

Respectfully submitted,

ROGER S. BALDWIN,
Attorney for Annie M. Pfeiffer,
120 Broadway,
New York City, New York.

Dated: April 30, 1937.

APPENDIX.

Revenue Act of 1928:

Section 115. DISTRIBUTIONS BY CORPORATIONS.

(f) *Stock dividends.*—A stock dividend shall not be subject to tax.

(g) *Redemption of stock.*—If a corporation cancels or redeems its stock (whether or not such stock was issued as a stock dividend) at such time and in such manner as to make the distribution and cancellation or redemption in whole or in part essentially equivalent to the distribution of a taxable dividend, the amount so distributed in redemption or cancellation of the stock, to the extent that it represents a distribution of earnings or profits accumulated after February 28, 1913, shall be treated as a taxable dividend. In the case of the cancellation or redemption of stock not issued as a stock dividend this subsection shall apply only if the cancellation or redemption is made after January 1, 1926.

Revenue Act of 1936:

Section 115 (f) (1). GENERAL RULE.

A distribution made by a corporation to its stockholders in its stock or in rights to acquire its stock shall not be treated as a dividend to the extent that it does not constitute income to the shareholder within the meaning of the Sixteenth Amendment to the Constitution.